RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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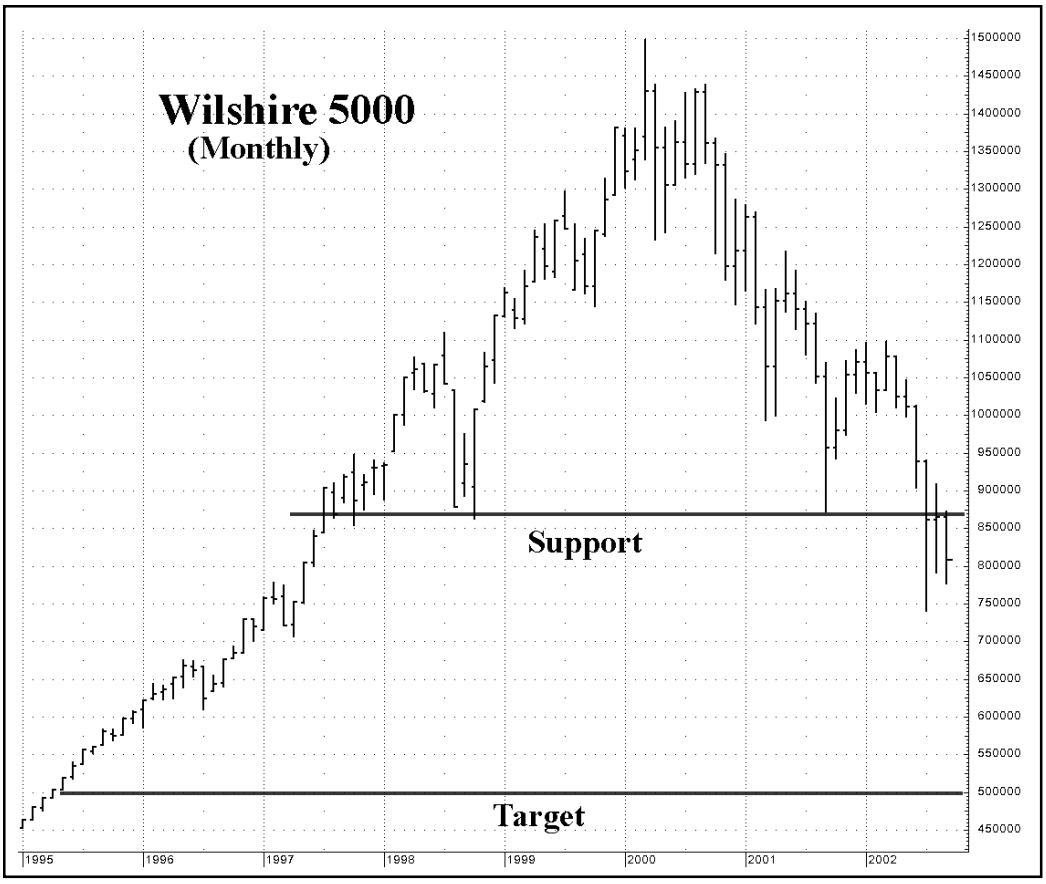
Sept. 13, DJIA 8312.69; PTI 5247; A-D Ratio -2.58
Sept. 20, DJIA 7986.02; PTI 5234; A-D Ratio -3.97
Sept. 27, DJIA 7701.45; PTI 5227; A-D Ratio -4.42
S&P Yield: 1.91% S&P p/e: 30.95
Gold 50-Day MA: 315

WILSHIRE 5000 – The Wilshire 5000 (actually 6,000 stocks) covers a large percentage of US stocks including stocks on the NYSE, the Amex and the Nasdaq. The Nasdaq translates into dollars. At its high recorded on March 24, 2000, the value of the Wilshire was 14754 or $14.7 trillion dollars. At its recent bear market low of 7396 struck on July 24, 2002, the Wilshire was down 49.8%. This means that at its July low the average stock had lost roughly half its value.

This monthly chart of the Wilshire shows that this index has traced out a huge head-and-shoulders top formation. When the Wilshire broke below support (the higher horizontal line) we had a plunge and then a more recent rally-consolidation. The lower horizontal line shows the target or downside "count" following the break of the H&S formation. I put this target area at around 3000 to 4000. If this occurs, it would mean that the stock market had wiped out around 80% of all stock values since the year 2000 highs.



Admittedly, this would amount to horrendous losses in the greatest bear market since the early '30s. You may not believe this is possible, you may argue with this analysis, but the chart most definitely opens up this possibility.

How the Wilshire works its way down to the 3000-4000 area is another story. I believe it could take another two or three years to get there. And I believe the path down will be convoluted with one major upside correction before the final bottom.

JUST WRITING – Freud once wrote that artists and writers were fortunate. They could project their fantasies in the form of paintings or stories and actually make a living in that way. Imagine, making a living from your fantasies. I started out wanting to be a writer. I really believe that if I wasn't doing what I'm doing now, which is writing about the stock market, that I'd be writing fiction, maybe writing for Hollywood or for TV or some other such fantasy factory. Maybe it was fate, maybe it was from some other experience that set me off on this course, but today I find myself writing about the stock market or I should say writing about markets – and well, about other things as well.

I don't have any secrets. To tell the truth, I hate secrets. I'm fascinated with reality, with the truth, with how things work and what makes people tick and what makes markets move and what's happening in the world – what's **really** happening. What I do in this business is no secret. I've said that I have 8,000 subscribers, and the great majority of you, my readers, pay $250 a year to read my thoughts and my studies and my occasional fantasies. And I don't have a lot of overhead in this business, because I do all the writing myself, and I have three charming ladies who run the business.

One is my ex-wife, Paula, so you know we are good friends. Another is Pam, who started with me in her twenties, and (blush) that was about a quarter of a century ago. The third lady is Shell, who's been working for me for about three years, and seems to like the job. So yeah, I make enough money (you can figure it out yourself or get pretty close), but the money comes more as a sideline. What I like to do these days is write.

I'm 78 years old now, and I no longer like to travel, and I stopped riding motorcycles about five years ago, because traffic is getting pretty dense here in San Diego. No, the real reason I stopped is that my trainer told me that if I get in an accident with my old bones, there's a good chance that I'd never be the same. It's different when a 21 year-old kid cracks up rather than when a 78-year old man hits a cement wall. I had to concede that he was right, so I sold my Harley and stopped riding. I don't regret it. I rode from the age of 25 to the age of 74, and that's enough.

The study of markets and investments is simple and it's complex. It's simple because basically stocks go from very undervalued to very overvalued and then back to undervalued again. The study is complex because people don't believe stocks are a "buy" when they're undervalued, and people don't believe stocks are a "sale" when they're overvalued. And of course there's a lot of stuff that happens between undervaluation and overvaluation.

I write about the simple, and I write about the complex. And despite complaints from some of my subscribers, I write what I want (at my age, you're allowed to do that). A lot of the stock market has to do with emotions. I've always said that 90% of all the decisions that people make about investing, and yes, about everything in life, are based on emotions. God gave us the ability to think, to ponder, to study, but most of us neglect that side of us, and we operate on our emotions. That's where my writing ability comes in. I do think I'm a pretty good writer, and although I do a lot of thinking, I have learned to write like a writer, meaning that I've learned to appeal to people's emotions.

I don't write like a Wall Street analyst or an accountant or a lawyer. I write the way I talk or the way I think. The truth is that I write the way I would have if I was writing plays or movie scripts. Because, what the hell, that's the way life is. Why write in some esoteric, stilted way when you can just write the way you talk? Anyway, that's the only way I do write, and people seem to like it, so I keep doing it. It's as simple as that.

And you might ask, "What's a 78 year old guy doing sitting down every day studying the market and reading ten newspapers and thinking about the market and the world and God knows what? What's an old guy like you doing all that for, when you could be traveling, you could be out playing golf, or you could be sitting in a retirement home boring some other old guy about your experiences during World War II?"

The truth is that I'm doing what I like to do. I'm thinking about the world, I'm thinking about the markets, I'm writing what

I want, and damned if I'm not being paid well while I'm doing it. The fact is that I like, no I love what I'm doing, and it gives me a purpose in life. The markets excite me, they fascinate me, and the markets entail everything that goes on in the wide, wide world. To my mind, there's nothing more exciting and fascinating than the markets. When some stock surges higher, there's a story behind that move. When lumber goes down the limit, there's a story behind that move. When some giant stock like General Motors tops out, the market is "talking" to us. The language of the market is amazing, because it's the most prescient or far-seeing language there is. There's just nothing like it.

I'm greedy, I want to know everything before it happens. Don't ask me why, I just do. And by far the best way to get to that extraordinary place is through the markets. That is, if you'll take the trouble to understand and believe the language of the market. You see the market is always talking, but very few take the trouble to learn the language of the market.

No, the strange part of it is that arrogant or ignorant analysts study everything else except market action. They study statistics and earnings statements and news (most of this stuff is really history, because all news is history). They mistakenly believe that these stale studies will tell them what the market is going to do or what some stock is going to do – or even what the economy is going to do.

The market is its own best forecaster, but you must learn the language of the market. I study what the market is saying, and if I'm lucky sometimes I get it right, and at other times, damn it, I mess up. I keep hoping that I can get it right better than half the time, and I keep hoping above all that I get the long-term trends right. But I keep trying, and it's always sort of a thrill if I can get the story at least partly right.

Don't ask me why, but there never were many people who were any good at reading the language of the market. The reason, I believe, is that the language of the market is counter-intuitive. Most of the time it's emotionally difficult to believe what the market is saying. The market is like that – it loves secrecy, it loves to hide its real meaning. The market loves to confuse the crowd, often because what it's saying it not what the crowd wants to hear. For instance, when the market wants to go up, it somehow acts as though the market is a very dangerous place to be, and you wouldn't touch stocks with the proverbial ten-foot pole. And when the market wants to go down, it acts as though the best place in the world to be – is to be loaded with stocks.

Anyway, that's how I spend a lot of my time – writing about that old devil market. And the amazing thing is that I get paid for writing about this devil. The most pleasant thing about my business is that if I'm right (and I'm right some of the time) I'm either helping people make money or I'm keeping people from losing their money. And c'mon, what's wrong with that?

What about money? Yeah, we all know that you need money to buy the things you need in your daily life. Most people work hard for their money. Me, I like money to work for the people I write for — my subscribers. You can either work for money or you can let money work for you. Most people work for money, and then they lose it in the stock market or at Las Vegas or in some damn-fool business venture. Most people, not all of them, but most of them do something along those lines.

I tell my kids that the great thing about money is that it allows you to be free. That's what I like about money, it allows you to do most of the things you want to do. Not all, of course, but most of those things. And here's the irony for me. I don't like to do most of the things that money will buy. Maybe it's just that I'm 78 years old, and I've already done a lot of the adventurous things. I leave the adventures to my kids. Just hearing about what they're up to – is adventure enough for me. I've got a son who's been traveling around the world for a year, I've got a daughter who will graduate from U of Arizona in December, and I've got two more daughters who have five kids between them. And I've got an ex-wife who's living with my autistic daughter in Hawaii — and last but not least, I've got a second ex-wife (we're great friends) who runs my office.

And I've got a wife who's 32 years younger than I am, and we've been married for 17 years. We lived together for two years, but being married is better, you've got more of a commitment, I was just as committed when we lived together. My wife Faye is about the smartest woman I've ever met, and I've met a lot of smart women. Faye's a corporate lawyer, and she knows more about corporate law and finance and structure than I ever will. And she knows a lot about markets, but she's just not fascinated with markets the way I am, and she's never learned the language of markets. She's just not that interested.

But I'm fascinated with her mind, and I have reason to believe that she is interested in my mind. Actually, I think we're soul mates. I've heard that each person has seven potential soul mates somewhere in the world, and you're lucky as all get-out if you happen to run into one of them. And I believe it. Faye and I hit it off on our first date. In fact, after our first date we never parted. That's how I know we are soul mates.

So how do you know whether you've met your soul mate? You know, you know in five minutes, you just know. Most people, I believe, never meet their soul mates. When that happens they eventually tire of each other and end up getting divorced. Others just stay together because well, if feels safe. But soul mates stay together because they are fascinated with each other. It's more than giddy romance. They're crazy about each other. In marriage I found out one thing. It's not enough to like each other. You've got to be crazy about each other. You've got to be excited about seeing each other. If you're not, then you're not married to a soul mate. And that's all I have to say about marriage.

Hey, all the above, it isn't what you've been paying me for, is it? Well, maybe it is. After all, you remember what I said about 90% of all decisions are made on the basis of emotions. Well, if you don't know anything about me, if you don't have at least some kind of emotional feeling about me, then why the hell would you want to believe what I say about the markets? When I read what some other analyst is saying about the market, in the back of my mind I'm thinking, who is this guy or who is this gal? Is she "all together"? Is he really intelligent? Is he communicating or just ranting? Would I trust this guy with my money? Why is he writing? Does he really believe what he's saying, or is he just doing it because it's a job and it's a living?

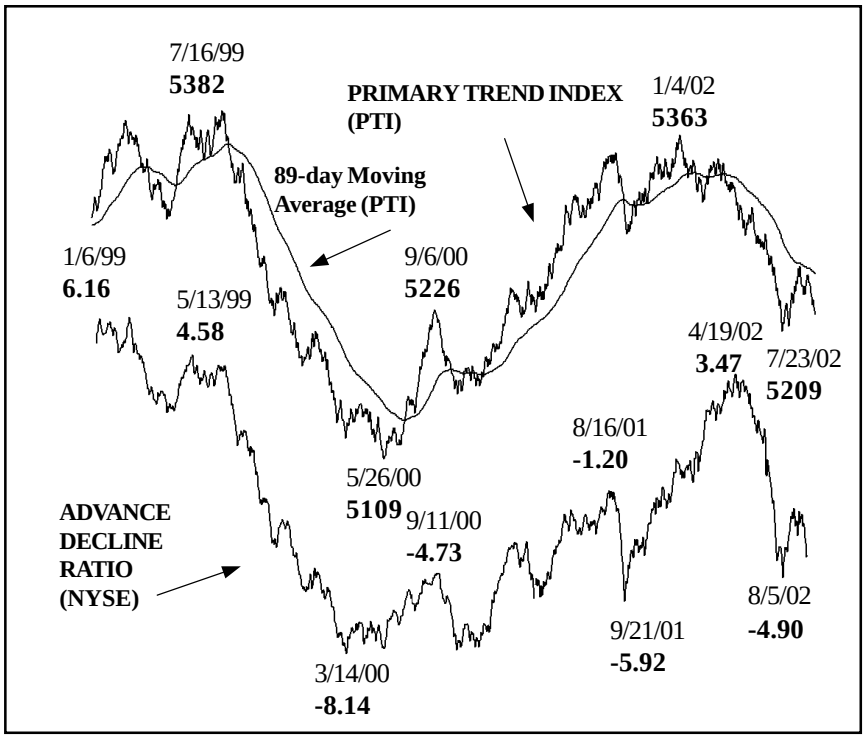
I hate that word "job." I've had jobs. I spent six months when I was age 16 loading trucks. That was a job — it was my first job, and I had to join a union to get that job. But it was interesting, because it was a real job and the Depression was still on. But I didn't love the job. Later, after the War I spent ten years as a textile designer, that was during the '40s and '50s, and what made that job interesting was that I was making $18 thousand a year during tough times. But I didn't love that job, I loved the money.

OK, enough, let's talk about the markets. After four years into this bear market, and after huge losses to investors, about $8 trillion dollars in losses, one incredible fact emerges. The incredible fact is that people and corporations are still unaccountably complacent. It's as if investors don't know what's hit them.

As I write everyone seems to be waiting for the bottom. People don't want to sell their stocks because they've been told that they're "holding for the long haul." "Over the years," they've been told, "stocks go up."

Sure, stocks go up, but it all depends where you bought those stocks and what time frame you're talking about. If you bought your stocks at the 1929 highs sure stocks go up, but it took a quarter of a century before your stocks went to new highs. That's twenty-five years of waiting before you started making money. Of course, if you had bought your stocks three years later in 1932 then your stocks really went up, but they started up in 1932, and there's the difference.

The most money is made if you can time the market successfully. The only problem is that very few people can do that. If you bought all your stocks at the beginning of a bull market, and you sold at the peak area of the bull market, and then you stayed out of the following bear market, that would be the best way to handle your money. But as I said, that's a very



difficult thing to do. It involves a lot of study and the ability to move when the trend changes. Very few people are capable enough or gutsy enough to do that.

Next – where do I think this market and this economy is going? The truth, I think both the market and the economy are going into the tank. This bear market, so far, has been the worst since World War II, but I think before this bear market is over it's going to be the worst since 1929-32. I think we're going into a deflationary mess. I base this partly on the recent and current absurd valuations. I base it on the many bubbles, some having burst and some (houses, mortgages, debt) still in place. And I base it on the incredible complacency that has accompanied the bear market so far.

I keep talking about 90% downside days. What is a 90% day? A 90% downside day is a day when downside volume is 90% of the total of upside volume plus downside volume. And it also includes downside points being 90% of the total of upside points plus downside points. In other words, a 90% downside day is a panic day. Most declines of the past have included a series of 90% downside days. For instance, in the year 1974 we had eight 90% downside days. I mean people were panicky in 1974. In the years 1999 through 2002 do you know how many 90% downside days we've had? Four, none in 1999, one in 2000, two in 2001 and just one in 2002, that one occurring on September 3 of this year.

Here's this bear market in force since September 1999, here's the Nasdaq collapsing, here's the Wilshire 5000 falling in half, here's $8 trillion in market values wiped out – and we've had four 90% downside days, and only one so far this year!! What does that tell you? It screams of complacency. I'll tell you what else it tells me. It tells me that the bear is going to make up for lost time. It tells me that somewhere ahead, we're going to see one hell-raising, panicky series of 90% downside days. It tells me that the real panic declines lie ahead.

LATE NOTES AND OBSERVATIONS – These are the Dow Jones Industrials end-of the month closings.

March — 10403.94
April — 9946.22
May — 9925.25
June — 9243.26
July — 8736.59
August — 8663.50

If the Dow closes below 8663.50 on Monday the Dow will have been down for six months in a row. To my knowledge, this has been surpassed only once before in history. What does it mean? For one thing, it tells me that this is fated to be an historic bear market, and that what we've seen so far may be the preamble – a taste of what may lie ahead.

I would also think that six months in a row on the downside suggests an oversold stock market. Of course, big bear markets can do strange things, and this bear market is following the greatest bull market, the most speculative bull market in US history. So an incredible series of six declining months in a row suggests a market that may be sold out, I also believe that this is a bear market that should not be "fooled around" with.

A lot of smart traders have already been chewed up trying to out-trade this market. I don't recommend "messing with the bear." My suggestion is that you take a conservative position in Treasury notes of up to ten year maturities and add gold and gold shares as insurance in case the US dollar hits the skids.

GOLD – I've explained that gold is in a primary bull market, and further that gold is in the early stages of a primary bull market. This "first phase" is the difficult phase. It's particularly difficult because gold, real money, threatens the manufacturers of fiat or "paper money." The manufacturers of phony money are the central banks of the world and their recently knighted leader, Alan Greenspan.

The basis of the central banks is their insistence that the legal tender paper that they issue be considered as real money. Gold stands in the way of the central banks and their paper. For a whole generation the central banks have issued their propaganda to the effect that paper is real money and gold is an ancient relic good for filling teeth or making senior class rings.

I include on this page a weekly chart of gold. This chart traces the up-trend that started for gold in January 2001. Note that despite what you may think or "feel," gold has been pressing against the upper side of its rising channel. Thus gold has been acting well, and it's even entitled to "rest" a bit.

FINAL THOUGHTS – The great danger to investors, and to everyone else for that matter, is deflation. And the great danger with deflation is that it impacts cruelly on debt. This nation is now swimming in debt to a total estimate (all classes) of $38 trillion. The problem is that if deflation hits (and it's already hitting) debt becomes difficult, and in many cases, impossible to handle.

The Fed is aware of this, and it's doing everything in its power to ward off deflation. To do this the Fed must bring short rates below the inflation rate. But if inflation turns to deflation, the Fed is rendered powerless. It can't bring its rates below zero.

If the US goes into net deflation, I foresee a veritable blizzard of bankruptcies and foreclosures. In fact, the dollar itself then becomes suspect. There is only one money that is not someone else's IOU, and that money is the only money with inbuilt intrinsic value; that money is gold. Gold is the only financial asset that cannot default. In a deflation, gold becomes the ultimate island of safety. A possible second is gem-grade diamonds.

Next Mailing: October 23, 2002